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IN THE

Supreme Court of the United States

Nos. 510, 511. October Term, 1929.

S. O. WYNNE, Federal Prohibition Administrator for Eastern Pennsylvania, et al.,

v.

SWANSON CHEMICAL CORPORATION.

JAMES M. DORAN, Prohibition Commissioner of the United States, et al.,

v.

MARTIN H. CASPER, Trading as DELMAR MANUFACTURING AND CHEMICAL COMPANY.

On Certificates from the United States Circuit Court of Appeals for the Third Circuit.

Brief for Appellee Below.

PATRICK J. FRIEL,
Attorney for Appellee.

International, 236 Chestnut St., Philadelphia

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No. 510.

S. O. WYNNE, FEDERAL PROHIBITION ADMINISTRATOR FOR EASTERN PENNSYLVANIA, ET AL.,

v.

SWANSON CHEMICAL CORPORATION.

No. 511.

JAMES M. DORAN, PROHIBITION COMMISSIONER OF THE UNITED STATES, ET AL.,

v.

MARTIN H. CASPER, TRADING AS DELMAR MANUFACTURING AND CHEMICAL COMPANY.

On Certificates From the United States Circuit Court of Appeals for the Third Circuit.

BRIEF FOR APPELLEE BELOW.

PRELIMINARY STATEMENT.

The question presented in this case differs somewhat from others of the several cases to be heard before this Honorable Court pursuant to certificates submitted by the Circuit Court of Appeals for the Third Circuit in that in this

particular case the appellee below had never issued to him a liquor permit as the term is defined in the National Prohibition Act, but had, on the contrary, a permit issued to manufacture an article which is specifically exempted from the operation of the Prohibition Act by the provisions of Section 4, Title II of said Act, and at no time did the appellee below ever have in his possession or authority to use anything but specially denatured alcohol which is a non-beverage, non-potable article.

Inasmuch as the question presented is somewhat novel and in view of the further fact that the companion cases to be heard have had in the preparation thereof, considerable attention given to the decided related cases, this argument will be addressed and confined solely to a differentiation between this particular class of permit and the other classes of permits and an attempt made to distinguish between them.

ARGUMENT.

The appellants in the brief submitted to the Court have phrased five questions as being for this Court to pass upon, none of which accurately present the question as decided by the District Court below. Therefore, the appellee restates the question, as he sees it, to be as follows:

> CAN THE COMMISSIONER OF INTERNAL REVENUE CANCEL A PERMIT REGULARLY ISSUED WITHOUT LIMITATION AS TO TIME THROUGH THE MEDIUM OF A REGULATION AND WITHOUT PROCEEDING ACCORDING TO THE PROCEDURE OUTLINED FOR REVOCATION OF PERMITS AS CONTAINED IN SECTION 9 OF TITLE II OF THE NATIONAL PROHIBITION ACT?

The Commissioner of Internal Revenue and his agents have been since 1924 attempting to secure the power to revoke by regulation, through the medium of a regulation requiring the so-called article permits to be annually renewable and the right to refuse such renewals, and thereby effect a revocation without proceeding in the form of a citation and hearing.

The question which accordingly arises from this situation has been repeatedly passed upon by the District Courts of the United States in practically every district and with the almost unanimous result that such powers were deemed by the courts as not having been vested in the Commissioner.

In order that the Court may get some idea of the overwhelming number of decisions on this point which have decided that the Commissioner has no such power, the Court is referred to the following reported cases.

Fred Feil Brewing Co. v. Doran, 2 Fed. (2) 879;
Stroh Products Co. v. Davis, 8 Fed. (2) 773;
Smith v. Foster, 15 Fed. (2) 115;
Gautieri v. Sheldon, 7 Fed. (2) 408;
Weste v. Campbell, 21 Fed. (2) 771;
Higgins v. Foster, 12 Fed. (2) 646;
Glenwood Industrial Distilling Co. v. Doran, 30 Fed. (2) 878;
Mascola v. Mellon, 25 Fed. (2) 173.

Not only have the foregoing cases been reported on this very point, but there have been in the various districts other cases unreported to a like effect and in the District of Columbia alone, there are to counsel's knowledge some twenty or more cases on the same point.

The Court is advised that the permits here in question are not liquor permits, in the strict sense of that term, nor are they beverage permits since the products dealt with by such permits are made from specially denatured alcohol

which is in itself non-potable and unfit for use for beverage purposes, and the articles themselves as well as the ingredients thereof are not subject to the operation of the National Prohibition Act because they are specifically exempted from such operation by the provisions of Section 4, Title II of the National Prohibition Act which provides as follows:

> Sec. 4. The articles enumerated in this section shall not, after having been manufactured and prepared for the market, be subject to the provisions of this Act if they correspond with the following descriptions and limitations, namely:
>
> (a) Denatured alcohol or denatured rum produced and used as provided by laws and regulations now or hereafter in force.
>
> (b) Medicinal preparations manufactured in accordance with formulas prescribed by the United States Pharmacopœia, National Formulary or the American Institute of Homeopathy that are unfit for use for beverage purposes.
>
> (c) Patented, patent, and proprietary medicines that are unfit for use for beverage purposes.
>
> (d) Toilet, medicinal, and antiseptic preparations and solutions that are unfit for use for beverage purposes.
>
> (e) Flavoring extracts and sirups that are unfit for use for beverage purposes, or for intoxicating beverage purposes.
>
> (f) Vinegar and preserved sweet cider.
>
> A person who manufactures any of the articles mentioned in this section may purchase and possess liquor for that purpose, but he shall secure permits to manufacture such articles and to purchase such liquor, give the bonds, keep the records, and make the report specified in this Act and as directed of any liquor commissioner. No such manufacturer shall sell, use, or dispose of any liquor otherwise than as an ingredient of the articles authorized to be manufactured there-

from. No more alcohol shall be used in the manufacture of any extract, sirup, or the articles named in paragraphs b, c and d of this section which may be used for beverage purposes than the quantity necessary for extraction or solution of the elements contained therein and for the preservation of the article.

Any person who shall knowingly sell any of the articles mentioned in paragraphs a, b, c and d of this section for beverage purposes, or any extract or sirup for intoxicating beverage purposes, or who shall sell any of the same under circumstances from which the seller might reasonably deduce the intention of the purchaser to use them for such purposes, or shall sell any beverage containing one-half of 1 per centum or more of alcohol by volume in which any extract, sirup, or other article is used as an ingredient, shall be subject to the penalties provided in section 29 of this Title. If the commissioner shall find, after notice and hearing as provided for in section 5 of this Title, that any person has sold any flavoring extract, sirup, or beverage in violation of this paragraph, he shall notify such person, and any known principal for whom the sale was made, to desist from selling such article; and it shall thereupon be unlawful for a period of one year thereafter for any person so notified to sell any such extract, sirup or beverage without making an application for, giving bond, and obtaining a permit so to do, which permit may be issued upon such conditions as the commissioner may deem necessary to prevent such illegal sales, and in addition the commissioner shall require a record and report of sales.

The Court is particularly asked to note subdivisions (a) and (d) of said section for the reason that subdivision (a) exempts denatured alcohol which is in accordance with the interpretation of the Act not a potable beverage article, but which is the chief ingredient of the articles enumerated in subdivision (d) of said section and stress is laid upon this particular portion of the National Prohibition Act for the reason that it is immediately followed by Section 5 which deals with an abuse or misuse of the preparations

enumerated in Section 4 and wherein it is provided that should the Commissioner find that any of the articles therein enumerated do not correspond with the descriptions and limitations outlined, the Commissioner may by a citation proceedings, cite such person to appear and show cause why his permit to manufacture and sell such articles should not be revoked, in the event that it is determined upon analysis that same shall be dealt with as an intoxicating liquor. The very phraseology of the section quoted is sufficient to indicate that Congress intended a distinction between beverage and non-beverage products and the further fact that Congress devoted an entire Title, i. e. Title III of the National Prohibition Act to the subject of industrial alcohol and indicated its desire to "place the non-beverage alcohol industry and other industries using such alcohol as a chemical raw material or for other lawful purpose upon the highest possible place of scientific and commercial efficiency consistent with the interests of the Government, and which shall insure an ample supply of such alcohol and promote its use in scientific research and the development of fuels, dyes and other lawful products," is quite indicative of such intent. This provision is quoted as well for the purpose of showing the intent of Congress to deal liberally with industrial alcohol as for the purpose of comparing such expressions with that quoted by the appellants in Section 3 of Title II of the National Prohibition Act which the Court will note refers to the use of intoxicating liquor as a beverage.

Not only have the District Courts of the United States overwhelmingly refused to sanction the exercise of power in this respect as sought by the Commissioner but the United States Circuit Court of Appeals for the Second Circuit in the case of **Higgins v. Foster, 12 Fed. (2d) 648** has said:

> "We think that Section 6 of Title II has no relation to denatured alcohol and that there is therefore no statutory provision which sets a term to such permits,

whether they be assumed to be authorized by Section 4 of Title II or Section 13 of Title III under which Article 21 of Regulation 61 was promulgated by the Commissioner. Section 6 uses the word 'liquor' which is defined by Section 1 of Title II and which seems to us clearly to be confined to beverages. It is true that it uses the word, 'alcohol,' but that especially in its context precludes denatured alcohol which is not potable. Hence we think that the permit in its original form was not unlawful and that the regulation of November 14, 1925, did more than confine permits for denatured alcohol to the terms prescribed by statute."

and the Court further commenting upon the limitation of permits and procedure for cancellation thereof said:

"Again we do not think that by originally making the permit terminable by cancellation the commissioner could evade, or meant to evade, Section 9 of Title II assuming for the moment that that section applied to them. In effect it had as indefinite duration, and was subject only to such revocation as the law allowed. It did not lie within the power of the commissioner by phrasing the permit in the language chosen to escape any requirements of cancellation which the statute imposed."

and reasoning further, the Circuit Court of Appeals in that case held:

"Moreover, if Section 9 of Title II applies to permits for denatured alcohol, we cannot see that the commissioner under the guise of legislation may do in gross what he had no power to do in detail. If each holder of a permit was entitled to insist upon a hearing before revocation, it would as much take away his right so created to cancel along with his own the permits of all others similarly situated, as though the action had been directed towards him alone. No reason is suggested why it should be possible by so multiplying the wrong to give it a character of legality.

"THEREFORE the question comes to whether Section 9 of Title II applies to denatured alcohol. We thing that it does. It is clear that in spite of its head-

ing Title II covers more than potable intoxicants. Section 4 describes non-potable liquids exclusively with the exception of cider and especially mentioned denatured alcohol (sub. div. a). It provides for a permit to manufacture and in other ways regulates dealing in them. Section 5 concerns the products mentioned in Section 4 and prescribed the procedure to revoke permits granted under it, but it is limited to defects in the quality of the products themselves. But it is not to be supposed that Section 4 was the measure of the commissioner's power to proceed against holders of permits under Section 4. Other abuses were possible than defects in quality and might be equally intolerable or more so. On the other hand we should expect that the procedural protection given holders of permits by virtue of Section 5 would not be taken from them when charged with other abuses in the conduct of their business. In short, we should look for a provision beyond Section 5 under which such permits might be revoked, but without opening the door for arbitrary and unreviewable action."

However, the Commissioner is apparently not satisfied with the machinery set up in the Act for the purpose of revoking permits of those who have violated the terms of the regulations or permits, but he has in mind a more summary proceeding whereby, the holder of a permit, at the whim of the Commissioner might have his permit revoked, cancelled and terminated through the expediency of a refusal to extend it upon grounds which may be imaginary, trivial or even based upon personal malice. The procedure sought by the Commissioner as a method of revocation would deny the permittee a right to a hearing, upon such charges as the Commissioner might hold against him, and deny a fair trial of the respective merits of the Commissioner's position and that of the permittee. He would again depend upon the whim of the Commissioner as to whether or not he might have a hearing because the Act itself provides for no such procedure as a hearing upon a disapproved application. The only provision of the Act with reference

to a trial in the event of a refusal of an application by the Commissioner is contained in the last paragraph of Section 6 of Title II which is as follows:

> "In the event of the refusal by the Commissioner of any application for a permit, the applicant may have a review of the decision before a Court of Equity in which manner provided in Section 5 hereof."

and the manner provided in Section 5 with reference to review by Courts of Equity in connection with decisions of the Commissioner is as follows:

> "The manufacturer may by appropriate proceeding in a Court of Equity have the action of the Commissioner reviewed, and the Court may affirm, modify, or reverse the finding of the Commissioner as the facts and law of the case may warrant."

It will be noted, therefore, that nowhere in the Act is there any provision for a departmental hearing upon disapproved or refused applications and the practice of conducting such hearings on disapproved application is not a procedure provided for by law and therefore a right to which the permittee or applicant is entitled. It is simply an outgrowth of practice developed by expediency in connection with these cases and may be terminated by the Commissioner at any time without violation of the statutory requirements.

The law has, however, provided for the cancellation of permits in a definite form which is by way of citation upon charges and hearing thereon in accordance with the machinery outlined in Section 9 of the Act which method the Commissioner seeks to circumvent for reasons of his own and aspires to the position which would enable him to legislate by regulation.

The placing of regulatory power in any department of the Government or bureau thereof has inevitably led to the attempt to create laws by regulation and this evil as practiced by certain branches of the Government is often a

misuse of the power which it was intended to confer upon officials of the Government. They take the position that an approval of a regulation by the Secretary of the Treasury gives that regulation the force and effect of a constitutional enactment.

The procedure sought to be established by the Commissioner and his agents is without parallel in the attitude of the law toward other legitimate businesses, the implication being that every holder of an alcohol permit is a potential criminal and the aspersion necessarily casts an insult upon all the industrial and scientific users of alcohol in the country. Were the Commissioner to have his way he would doubtless hold that there is absolutely no need for the legitimate use of alcohol in any event and he would demand regulation upon regulation until he had reduced every bona fide holder of an alcohol permit to the level of a paroled convict. He believes the law should be made so that it would yield to the whim of the Commissioner as expressed in his regulation from time to time, but the Court can doubtless perceive that such a thing is obnoxious to our constitutional guaranties and as has been said in Courts in connection with the Commissioner's ambition in this respect—this is a Government of laws and not of men and that legal principles are not to be sacrificed to mere matters of expediency.

The intent of Congress that the use of industrial alcohol should be placed upon the highest possible plane of commercial efficiency is not consistent with the wishes of the Commissioner that he be permitted to harass, embarrass, hinder and delay the use of industrial alcohol as an ingredient and essential element to the many useful arts and industries and the fact that industrial alcohol is a non-potable, non-beverage article when acquired by permit holders for legal use in legitimate business is one of the reasons why Congress differentiated between industrial alcohol and liquor for intoxicating beverage purposes as defined in Section 1 of Title II.

It is argued that specially denatured and toilet preparations containing more than one-half of one per cent. of alcohol by volume are liquor within the meaning of Sections 1 and 6 of Title II. The most complete refutation of this argument is contained in the italics supplied by the appellants in their brief wherein they state that certain articles are within the definition of liquor and which are "fit for use for beverage purposes." Nowhere in their argument have they stated that the specially denatured alcohol or toilet preparations manufactured pursuant to the permit here involved are "fit for use for beverage purposes." The very fact that Section 4 of Title II after enumerating certain of the articles exempted therein from the Act was a clear expression of fact that they were deemed unfit for beverage purposes and they cannot, by regulation, be deemed to be within the purview of the Act relating to intoxicating liquor, nor can the Commissioner by regulation extend, modify, or circumvent the Act by placing them within the operation of the Act.

The second argument advanced by the appellants, which says, in effect, that if the articles enumerated are held not to be within the definition of liquor as provided for in Sections one and six of Title II, that there then exists no provision for the review of the Commissioner's decision in reference to permits for such articles, is sufficiently answered by the provisions of Section 9 of Title II which does not limit in terms the kind or type of permits, the machinery for the taking away of which is therein contained and we again refer to the case of **Higgins v. Foster, supra,** wherein the application of Section 9 to denatured alcohol permits was passed upon and in further commenting upon the application of Section 9 to industrial alcohol permits, the Circuit Court of Appeals for the Second Circuit in that case said:

> "The language of Section 9 of Title II seems to us to bear out this expectation. It is not, like Section 6 confined to 'liquor', but speaks generally of permits covering all cases where 'any person who has a permit

is not in good faith conforming to the provisions of the Act.' It is quite true that a defect in the product, covered by Section 5, would fall within the compass of this general language, but the procedure of that section was special and that fact accounts, we think, for its presence alongside of Section 9, and relieves us from the embarrassment of assuring that it was redundant. In short, Section 9 protected all holders of permits, whether for potable or non-potable intoxicants while Section 5 prescribed a particular procedure in the case of non-potable permits when the fault lay in the quality of the product."

The third argument advanced by the appellants is sufficiently answered by proper interpretation of Section 6 since Section 6 deals with liquor permits as distinguished from industrial alcohol permits and the Circuit Court of Appeals for the Second Circuit has held:

> "We think that Section 6 of Title II has no relation to denatured alcohol and that there is therefore no statutory provision which sets a term to such permits, whether they be assumed to be authorized by Section 4 of Title II or Section 13 of Title III."

which latter Section we have quoted in connection with the intent of the Congress to place the non-beverage alcohol industry upon the highest possible plane of commercial efficiency.

The fourth argument advanced by the appellants is an attack upon the provisions of their own interpretation of industrial alcohol permits, since the Department itself originally recognized the distinction between liquor permits and industrial alcohol permits, because since the inception of permit procedure the Department followed the provisions of Section 6 with reference to limitation of time on liquor permits and placed industrial alcohol permits in another category without limitation, said permits to be in effect until surrendered by the holder or *until cancelled by the Commissioner of Internal Revenue for violation of the pro-*

visions of Title III of the National Prohibition Act, and this distinction is now attacked by the appellants for the reason that it is not consistent with their original interpretation. They now contend that the Congress intended that every permit be specifically limited as to time, but they point out no reason why the Congress didn't say that such was their intent since the Congress did specifically limit the duration of liquor permits. The only reason which they can truthfully and honestly advance for proposing that such permits be limited is that they intend to make use of matters of expediency as a basis for circumventing the Act itself. Since the law provides for the taking away of a permit in accordance with well defined procedure for any violation of law or regulation, the Commissioner has within his power the machinery for terminating the permits of those who have not in good faith conformed to the provisions of law and regulations.

Their fifth argument dealing with the validity of Article 118 of Regulation No. 2 and Article 113 of Regulation No. 3 is premised upon the fact that both classes of permits are within the definition of Section 6 of Title II of the National Prohibition Act. We take the position that Article 113 of Regulation No. 3 is not valid as a method for the termination of an industrial alcohol permit since the question was passed upon by the Circuit Court of Appeals for the Second Circuit and a similar regulation involved which led to the action in that case.

The Commissioner seeks to impose his *ex parte* judgment, as to the fitness or unfitness of an applicant, as a basis for his regulation and his proposed action, but the Commissioner's conclusion that a permittee is either fit or unfit to be the holder of an industrial alcohol permit is one that must be premised upon such permittee's compliance or non-compliance with the terms of the law and regulations.

In the event that from a proper premise the Commissioner concludes that a certain permittee is not conforming

to the law and regulation, that contention may be tried through the medium of the procedure as outlined in Section 9 which says in part that if at any time the Commissioner has reason to believe that any person who has a permit is not in good faith conforming to the provisions of the Act, that the Commissioner or his agents shall immediately issue an order citing such person to appear before him to answer the charges upon which the Commissioner has concluded that such a person is not a fit one to hold a permit.

The law is mandatory that the Commissioner shall immediately cite and specifically limits the return for the trial on such charges to a period not less than fifteen days nor more than thirty days from the service of said charges upon the permittee indicating very plainly the necessity of prompt action by the Commissioner to the end that undesirable permittees may be eliminated through the medium of revocation proceedings.

Certainly the Commissioner has within his power the method and the machinery for the cancellation of permits which are being abused and he should be compelled to employ the machinery provided. If the charges which the Commissioner seeks to press against any given permittee are material or substantial he can in a lawful manner prevent a misuse or abuse of permit privileges and the situation would not be that in which the general public would have the economic life or death of their enterprises in the hands of a possible autocratic or bureaucratic official.

Respectfully submitted,

PATRICK J. FRIEL,
Attorney for Appellee.